

STREAM ENERGY, INC.

IBLA 96-533

Decided October 20, 1998

Appeal from a decision of the Chief, Compliance Verification Division, Minerals Management Service, upholding an assessment of \$1,122.18 in late payment interest on underpaid royalties. MMS-95-0364-0&G.

Affirmed.

1. Federal Oil and Gas Royalty Management Act of 1982: Generally--Federal Oil and Gas Royalty Management Act of 1982: Royalties--Oil and Gas Leases: Assignments and Transfers--Oil and Gas Leases: Royalties: Payments--Rules of Practice: Evidence

Absent the assumption of the obligation to tender royalty payments by the unit operator, MMS properly looks to its lessee to satisfy late payment interest charges regardless of whether it was the lessee or the operator's error which caused the royalties to be understated.

APPEARANCES: Michael G. Underwood, Controller, Stream Energy, Inc., Oklahoma City, Oklahoma, for Appellant; Peter J. Schaumburg, Esq., Sarah L. Inderbitzin, Esq., Howard W. Chalker, Esq., Geoffrey Heath, Esq., and Lisa K. Hemmer, Esq., Office of the Solicitor, U.S. Department of the Interior, Washington, D.C., for the Minerals Management Service.

OPINION BY ADMINISTRATIVE JUDGE BURSKI

Stream Energy, Inc. (Stream), has appealed from a decision of the Chief, Compliance Verification Division, Minerals Management Service (MMS), dated June 24, 1996, upholding an interest assessment of \$1,122.18 for late payment of royalties. We affirm.

The record indicates that underpayments for certain Federal leases in which Stream was the lessee (080-019419-A and 080-019419-C) were discovered in an audit of leases in the Kettleman Hills North Dome Unit conducted by the California State Controller (Controller) under contract with MMS, pursuant to delegated authority under section 205 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), 30 U.S.C. § 1735 (1994). The audit covered the period January 1, 1990, through December 31, 1992.

The audit concluded that Stream had understated both the volume of residue gas sold from Federal lease 080-019419-C as well as the amount of crude oil sold from Federal leases 080-019419-A and 080-019419-C, thereby resulting in an underpayment of royalties. Insofar as the residue gas payments were concerned, the Controller concluded that Chevron U.S.A. Production Company (Chevron), who was the unit operator, had understated the volume amounts sold in information provided both to the purchaser and the unit participants, ultimately resulting in a royalty underpayment of \$2,103 by Stream for the period in question. See Letter dated Mar. 3, 1995 (Federal Lease 080-018418-C). With respect to crude oil sales during this period, the Controller found that Stream had "fail[ed] to report and pay royalties on its entire share of crude oil sold from the [unit]," resulting in a royalty underpayment of \$2,118. See Letter dated March 3, 1995 (Federal Leases 080-019419-A and 080-019419-C).

Stream duly paid the assessed underpayments. Subsequently, on April 24, 1995, MMS issued invoice GBIL 10940590 seeking \$1,122.18 in interest charges on late payments of royalties. 1/ Stream appealed this assessment to the Director, MMS, asserting that, inasmuch as the error involved was that of Chevron, 2/ it is Chevron, not Stream, who should be assessed any interest penalty. By decision dated June 14, 1996, the Chief, Compliance Verification Division, affirmed the assessment of interest against Stream. Stream thereupon appealed to the Board.

Stream essentially reiterates the arguments which it made before the Director, MMS. Thus, Stream notes that, because Chevron had underreported the volumes sold, Stream had received less money from the purchaser than it was properly owed and had tendered its royalty based on the amount which it actually received. When, subsequent to the audit, Chevron tendered the additional funds to Stream which it was owed, Stream had immediately submitted royalties based on the underreported production to MMS. Stream argues that it "acted only as an intermediary transmitter and properly discharged its obligation to make timely payment after the proceeds were received from Chevron." (Statement of Reasons at 1.) Relying on the fact that it never had the beneficial use of the royalty underpayments, Stream

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1/ We note that a review of invoice GBIL 10940590 indicates that it covers not only leases 080-019419-A and 080-019419-C, but also lease 080-019772-A. There is nothing in the record submitted to the Board which explains the relationship of any underpayment with respect to lease 080-019772-A to the two leases discussed in the text. We will, however, assume that the argument which Stream is making with respect to the assessment of interest for the underpayment of royalties on leases 080-019419-A and 080-019419-C are equally applicable to lease 080-019772-A. In any event, the small amount of money involved with respect to this lease (an assessment of \$2.32 in interest) would scarcely justify a detailed review of this assessment.

2/ While we note that the decision of the Controller assessing additional royalties for crude oil sales did not expressly find that Stream had submitted payments in reliance upon production figures provided by Chevron, we will, for the sake of argument, assume that such was, in fact, the case.

maintains that it should not be assessed interest thereon. Rather, Stream argues, any liability for interest should rest with the party who had made the mistake in the first instance, namely Chevron, the unit operator. Id. at 2.

In response, MMS notes that it is well established that the lessee is ultimately responsible for royalty payments due on production from its leases, citing Forest Oil Corp., 113 IBLA 30, 39 n.7 (1990); Jerry Chambers Exploration Co., 107 IBLA 161, 163 (1989); Supron Energy Corp., 46 IBLA 181, 192 (1980). See MMS Answer at 3-4. While acknowledging that a lessee may designate a third party to act for the lessee with respect to lease operations, including the payment of royalties, MMS maintains that this does not relieve the lessee of the ultimate responsibility for payment of royalty due on production from its leases. Id. Because Stream is the lessee in this case, MMS insists that it remains responsible for satisfying the late payment interest charges. We agree.

[1] Section 111(a) of FOGPMA, 30 U.S.C. § 1721 (1994), provides, in pertinent part, that "[i]n the case of oil and gas leases where royalty payments are not received by the Secretary on the date such payments are due, or are less than the amount due, the Secretary shall charge interest on such late payments or underpayments." Additionally, 30 C.F.R. § 218.54, which implements FOGPMA, further provides that "an interest charge shall be assessed on unpaid and underpaid amounts from the date the amounts are due." Since it is uncontested that a royalty underpayment occurred, the statute and regulations require that an interest assessment be made.

As noted above, Stream argues that it should not be assessed interest on the late payments since it was, in no way, culpable for the unit operator's (Chevron) failure to properly report sales volumes. The assessment of interest on late royalty payments, however, is not premised on penalizing the lessee. Rather, interest is assessed to compensate the United States "for the cost of replacing funds that are due but not timely paid." Paul DeCleva, Jr., 141 IBLA 199, 201 (1997).

Moreover, the law is well settled that the lessee is responsible under a Federal oil and gas lease for satisfying the royalty obligation and remains liable therefor, absent assignment of the obligation to pay royalty to another. See Mesa Operating Limited Partnership, 125 IBLA 28, 38-42 (1992); Phillips Petroleum Co., 121 IBLA 278, 284 (1991). In the instant case, while Chevron was the unit operator there is no assertion that it was assigned the obligation to tender royalty payments to MMS on Stream's behalf. Thus, it was Stream's obligation to timely pay the full royalty.

While we do not doubt that Chevron's miscalculations may have directly precipitated Stream's royalty underpayment of royalty due on residue gas, we have consistently held that errors of third parties, including agents of the Federal lessee, do not vitiate the obligation of the lessee to tender royalty on a timely basis. See, e.g., Oxy USA Inc., 125 IBLA 308, 311-12 (1993); Union Exploration Partners, Ltd., 112 IBLA 140, 141-42 (1989); Cotton Petroleum Corp., 112 IBLA 1, 3 (1989). While it may be true that

Stream never enjoyed the beneficial use of the underpaid royalties, it is equally true that the United States was wrongfully deprived of that use. In requiring the payment of interest by Stream, the United States is not seeking to disgorge unjust profits from Stream; rather, it is simply insisting that it be made whole.

Stream argues that it is Chevron who should be required to pay any interest assessment since it was Chevron who caused the underpayment in the first instance. Regardless of Chevron's culpability, the fact remains that it is Stream, not Chevron, who is the Government's lessee and it is, therefore, Stream's obligation, as lessee, to tender the correct amount of royalties due on production from its leases.

Stream's reliance on Chevron's production figures is the result of a contractual arrangement (the unit agreement) between Chevron and Stream. If Stream believes Chevron is liable to Stream for the interest payments assessed against it, Stream is free to proceed in the proper forum to obtain recompense for its payments of such charges. The United States, however, properly assesses its lessees (or those who have formally assumed responsibility for royalty payments) any interest accruing from the failure of those lessees to tender the correct amount of royalties on a timely basis. See Dugan Petroleum Corp., 107 IBLA 91 (1989).

Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 C.F.R. § 4.1, the decision appealed from is affirmed.

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James L. Burski  
Administrative Judge

I concur.

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James L. Bymes  
Chief Administrative Judge

